

[Auditor's Home Page](#)[List of Audit Reports](#)

## Table of Contents

<b>Executive Summary</b>	<a href="#">Click Here To View</a>	<b>i</b>
<b>Introduction</b>		<b>1</b>
Background		1
Scope And Methodology		8
Major Accomplishments Related To This Program		9
<b>Finding I</b>		
<b>The City's Procurement Card Program Has Weak Internal Controls Which Expose The City To Improper, Abusive, And Fraudulent Uses Of Procurement Cards</b>		<b>11</b>
The City Has Significant Exposure Due To A Lack Of Adequate And Documented Internal Controls To Minimize Improper, Abusive, Or Fraudulent Cardholder Uses Of Procurement Cards		12
Based Upon The City Auditor's Assessments, Finance Agreed To Implement Improvements To The Program's Internal Controls		14
Control Weaknesses Create An Environment Susceptible To Improper, Abusive, And/Or Fraudulent Procurement Card Purchases		15
Several Retirement Services Department Procurement Cardholders Making Travel-Related Transactions That Appear To Be Improper		19
Finance Should Lead The Effort To Strengthen Controls To Minimize The Risk Of Fraud, Waste, And Abuse		20
CONCLUSION		20
RECOMMENDATIONS		21
<b>Administration's Response</b>	<a href="#">Click Here To View</a>	<b>23</b>
<b>Appendix A</b>	<a href="#">Click Here To View</a>	
<b>Definition Of Priority 1, 2, And 3 Audit Recommendations</b>		<b>A-1</b>
<b>Appendix B</b>	<a href="#">Click Here To View</a>	
<b>Risk Matrix</b>		<b>B-1</b>

<b>Appendix C</b>	<a href="#">Click Here To View</a>	
<b>Vulnerability Assessment .....</b>		<b>C-1</b>
<b>Appendix D</b>	<a href="#">Click Here To View</a>	
<b>City Policy Manual – City Procurement Cards - Draft.....</b>		<b>D-1</b>
<b>Appendix E</b>	<a href="#">Click Here To View</a>	
<b>Memorandum – Accomplishments.....</b>		<b>E-1</b>

# Introduction

In accordance with the City Auditor's 2005-06 Workplan, we have audited the City's Procurement Card Program. We conducted this audit in accordance with generally accepted government auditing standards and limited our work to those areas specified in the Scope and Methodology section of this report.

The City Auditor's Office thanks the Finance Department (Finance) management and staff for giving their time, information, insight, and cooperation during the audit process.

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## Background

The City of San José participates in the State of California's CAL-Card Program. The State of California entered into a Master Services Agreement with US Bank, for VISA Procurement Card services, effective through December 22, 2006. US Bank provides the City with Visa Procurement Cards for the purchase of items, such as supplies, materials, or equipment.

Procurement Cards are a means of purchasing supplies, materials, and equipment expediently without the need of obtaining a purchase order. Procurement Cards are sometimes referred to as credit cards or P-cards. For the purpose of this report, we will use the term Procurement Cards in place of credit card or P-cards. Unlike traditional Procurement Cards, the Cal-Card Program requires the City to maintain added controls over Procurement Cards. The controls include several spending controls, such as restrictions on the type of merchants the card will accept, and a more defined reporting structure to oversee card transactions. The City currently maintains single purchase and billing cycle limits on all City Procurement Cards. In addition to dollar limits, US Bank requires a separate spending control based on merchant classification. This control prevents Cardholders from using the card at certain merchants. US Bank requires the City to designate Approving Officials for each cardholder or group of cardholders. The Approving Official is responsible for managing and monitoring CAL-Card activity. Approving Officials receive monthly statements specifying the cards used and amounts transacted in addition to the monthly statements sent to Cardholders.

*Program  
Administration*

Purchasing retains responsibility for administering the overall Procurement Card Program and making payments to US Bank. City departments with Procurement Cards are responsible for reviewing Cardholder transactions, approving monthly invoices for payment, and providing Finance with the appropriate documentation to process payment to US Bank.

*City Procedures*

The City maintains Procurement Card procedures and instructions for Approving Officials, which guide the City's Procurement Card Program. Procurement Card procedures provide guidance on the establishment of controls such as purchasing limits, purchasing restrictions, purchasing and invoice processing, monthly statement reviews, billing disputes, lost or stolen cards, and making changes to Cardholder information.

The Approving Official instructions provide guidance on Procurement Card authorizations, monthly statement procedures, disputing charges, departure of employees, requests for additional cards or changes, and lost or stolen Procurement Cards. The Approving Official instructions also provide restrictions on which type of merchants are allowed for use with each Procurement Card. The list below highlights some of the merchant category code options available to Approving Officials.

**Exhibit 1      List Of Merchant Category Codes**

<b>Merchant Category Code</b>	<b>Category</b>
A	Airlines
B	Vehicle Rental
C	Hotel, Motel
D	Courier Service
G	Mail Order Houses
H	Food/Dairy/Drug Stores
I	Restaurants
J	Discount/Department/Variety Stores/Miscellaneous
K	Misc. & Specialty Retail Stores
Q	Schools, Educational Services
R	Membership Organizations, Charitable & Social Organizations

Source: City Procurement Card Procedures.

*Purchasing  
Restrictions*

City procedures specify a number of purchase restrictions on the use of City Procurement Cards. Those restrictions include:

- Maximum of \$2,500 per transaction (or lower if stipulated by Approving Official);
- Maximum of \$10,000 per 30-day period per card (or lower if stipulated by Approving Official);
- Total purchase with tax cannot exceed single purchase limit of card;
- Purchase must not be split to circumvent procurement policies;
- The least expensive item that meets basic needs should be sought;
- No cash advances allowed;
- No services (courier, office machine repair, film development, etc.) over \$1,000 (for any service, vendor must be incorporated);
- No purchases of items carried in General Services store unless out of stock;
- No purchases of communications equipment such as pagers, cell phones, walkie talkies, etc.;
- No rentals except small rentals not exceeding a week in duration;
- No items available through Citywide open purchase order (such as office supplies);
- No machinery that requires a maintenance agreement;
- No items from a vendor with an established open purchase order for the Cardholder's department;
- No purchase of flowers, shower gifts, birthday gifts, etc. for fellow employees; and
- No purchases at Super Kmart (per Council Resolution #67706).

*Responsibilities Of  
Program Members*

Under the CAL-Card Program, the City designates Agency Program Coordinators, Billing Office, Dispute Officials, Approving Officials, and Cardholders.

- Agency Program Coordinators (APC) oversee the entire Cal-Card Program within the City, including the administration of new accounts, reporting, and payment

processes. The APC is responsible for developing procedures, providing training, and enforcing compliance to the City's procedures and the terms of the CAL-Card Master Service Agreement.

- Billing Office is responsible for authorizing timely payment to US Bank after verifying the accuracy of the invoices.
- Dispute Officials may be designated to review and follow-up on pending Cardholder disputes to ensure timely resolution. Often, the Agency Program Coordinator or Billing Office contact serves as the Dispute Official.
- Approving Officials are responsible for reviewing, approving monthly Cardholder Statements of Account to ensure each Cardholder complies with City Procedures, and that transactions are appropriate. The Approving Officials also reconcile each Cardholder statement of Account to the Approving Officials monthly summary report.
- Cardholder is an employee with a Procurement Card. The Cardholder reconciles and signs the monthly Statement of Account at the end of each billing cycle. They are responsible for keeping records of each transaction, and must complete the monthly reconciliation.

According to February 2006 information from US Bank, the City has two Agency Program Coordinators, 24 Billing Officials, and six Dispute Officials. Based on US Bank records, the City maintained 256<sup>1</sup> Approving Officials for 1,296 Cardholders with a total monthly spending capacity of \$8,300,000.

*Process For  
Obtaining A  
Procurement Card*

City procedures stipulate the process for obtaining a Procurement Card. The Approving Official designates an employee to have a procurement card. An employee completes a Request for Procurement Card form. The form does not require the employee to submit a reason for requesting the card. The Approving Official approves the request and determines the card limits and any merchant restrictions. The Approving Official submits the form to Purchasing, and the City's Agency

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<sup>1</sup> See footnote 4 on page 7 for an explanation on the number of Approving Officials.

Program Coordinator processes the request through US Bank. The Approving Official receives the card and provides the card to the Cardholder.

*Purchasing Process*

The Cardholder uses the Procurement Card to purchase items such as supplies, materials, and equipment in accordance with City procedures. The Cardholder is supposed to ensure that any purchase including tax does not exceed the purchase limits. Additionally, the Cardholder must retain receipts which include an authorization code, amount, brief description of items purchased, name on Procurement Card, and vendor information. The City procedures do not require pre-approval of the purchases.

*Invoicing Process*

US Bank produces a monthly Statement of Account which it mails to Cardholders that had transactions during the cycle month. Additionally, US Bank provides Approving Officials with monthly summary lists of Cardholders with Statements of Account. The Cardholder is supposed to review the monthly statement to determine that the Statement of Account is accurate, submit receipts and logs of purchases, sign the monthly statement, and forward this cardholder packet to their Approving Official. A Cardholder can deduct from the statement total, any charges that they will dispute using US Bank's Statement of Questioned Items form.

The Approving Official reviews the Cardholder packet for accuracy, evaluates expenditures and documentation, and signs the statement authorizing processing. Additionally, the Approving Official should ensure all Cardholders with transactions submit a Cardholder packet. The Approving Official forwards the signed packet to the department's fiscal unit for processing.

According to Finance, the fiscal unit verifies that the packet includes the proper signatures and documentation, and inputs the information into the City's Financial Management System (FMS). The fiscal unit creates an edit list in the FMS listing the payments for Procurement Card transactions and forwards the packets to Finance for payment processing.

According to Finance, Accounts Payable staff review invoice packets to ensure that appropriate supporting documentation exists. Finance staff reviews the packets for any unusual transactions such as split transactions and processes payment to US Bank.

US Bank provides incentives for quick payments and late charges for payments made after 45 days. US Bank provides a credit of 0.62 percent of invoice totals for payments made within one to seven days of the statement date.

*Overview Of  
Procurement Cards  
Transactions*

Exhibit 2 highlights the number of Procurement Cards by City Entity, the number of transactions, expenditures, and average expenditure per transaction for the July 2004 to November 2005 timeframe.



**Exhibit 2      Breakdown Of Procurement Card Transactions For  
The City By City Entity For July 2004 To November  
2005<sup>2</sup>**

<b>City Entity<sup>3</sup></b>	<b>Number Of Cardholders</b>	<b>Number Of Approving Officials<sup>4</sup></b>	<b>Number Of Transactions</b>	<b>Expenditure</b>	<b>Average Expenditure Per Transaction</b>
Environmental Services	140	21	5,761	\$1,909,434	\$331
Parks, Recreation, and Neighborhood Services	324	78	9,504	\$1,473,162	\$155
General Services	111	7	6,035	\$1,412,610	\$234
Police	189	49	4,133	\$946,353	\$229
Fire	65	2	2,736	\$791,227	\$289
Transportation	98	34	2,444	\$728,822	\$298
Airport	83	23	1,724	\$540,366	\$313
Library	80	7	1,205	\$248,009	\$206
Information Technology	11	1	445	\$202,657	\$455
City Manager's Office/Office of Emergency Services	21	1	811	\$194,898	\$240
Planning, Building, and Code Enforcement	21	2	836	\$192,916	\$231
City Clerk/Council <sup>5</sup>	25	1	765	\$158,463	\$207
Office of Economic Development	6	2	418	\$125,556	\$300
Public Works	13	1	382	\$122,030	\$319
Employee Services	32	8	383	\$112,943	\$295
Housing	13	1	323	\$82,335	\$255
Finance	24	4	238	\$68,310	\$287
Retirement	2	1	275	\$65,706	\$239
Office of Cultural Affairs	19	7	291	\$42,784	\$147
City Attorney	12	2	183	\$33,090	\$181
City Auditor	3	2	66	\$15,241	\$231
Independent Police Auditor	4	2	49	\$5,479	\$112
<b>TOTAL</b>	<b>1,296</b>	<b>258</b>	<b>39,007</b>	<b>\$9,472,388</b>	<b>\$243</b>

Source: As reported by US Bank electronic records.

<sup>2</sup> Number of Cardholders and Approving Officials represent a snapshot as of November 2005.

<sup>3</sup> According to the Redevelopment Agency, they retain one credit card outside of the US bank program. We did not audit their records.

<sup>4</sup> Two Approving Officials serve more than one City Entity. As a result, the City Entity does not maintain 258 Approving Officials, but rather 256. The database includes 72 cardholders across 16 City Entities with no listing of an Approving Official.

<sup>5</sup> Mayor and City Council data included solely for the purpose of highlighting the scope. City Charter Section 805 restricts our ability to audit the Mayor and City Council.

As shown above, from July 2004 through November 2005 City Cardholders initiated 39,007 transactions valued at \$9,472,388 in expenditures. Exhibit 3 summarizes City Procurement Card transactions by expenditure category from July 2004 through November 2005.

**Exhibit 3      Summary Of City Procurement Card Transactions  
By Expenditure Category From July 2004 Through  
November 2005**

<b>Expenditure Category</b>	<b>Number Of Transactions</b>	<b>Expenditure</b>	<b>Average Expenditure Per Transaction</b>
Wholesale Trade	15,836	\$ 3,418,311	\$216
Other	6,822	\$ 1,572,726	\$231
Office Services	2,946	\$ 1,034,927	\$351
Business Expenses	2,027	\$ 635,998	\$314
Misc. Retail Supplies	1,722	\$ 566,386	\$329
Office Supplies	2,175	\$ 418,275	\$192
Building Services	871	\$ 391,951	\$450
Mail/Telephone	1,162	\$ 370,364	\$319
Vehicle Expense	1,492	\$ 238,840	\$160
Hotels	701	\$ 229,434	\$327
Eating/Drinking	1,303	\$ 209,348	\$161
Airline	715	\$ 156,668	\$219
Auto/RV Dealers	308	\$ 84,165	\$273
Medical	529	\$ 56,495	\$107
Other Travel	200	\$ 41,880	\$209
Rental Cars	151	\$ 28,710	\$190
Retail Services	47	\$ 17,913	\$381
<b>TOTAL</b>	<b>39,007</b>	<b>\$ 9,472,388</b>	<b>\$243</b>

Source: US Bank electronic records.

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**Scope And  
Methodology**

Our audit objective was to identify the operational threats facing the Procurement Card Program (Program) and the administrative controls in place to prevent, eliminate, or minimize those threats. Specifically, we conducted a Risk Assessment and Vulnerability Assessment of the Program's operational threats and corresponding controls. Based on our Risk and Vulnerability Assessments, we identified several threats for which the Program had no corresponding controls in place.

To a limited extent, we reviewed US Bank for City Procurement Card electronic transaction information posted from July 2004 through November 2005 to identify potentially improper, abusive, or fraudulent transactions. Specifically, we sorted the number of transactions by merchant category and searched for questionable transactions based on merchant

description and merchant name, such as Jewelry, Watches, Clocks—Tiffany & Company. We judgmentally selected a sample of these transactions to verify Cardholder compliance with policies and procedures. We did not attempt to project the extent of improper, abusive, or fraudulent transactions based on our review.

In developing our Risk Matrix, we identified the potential threats associated with the City’s Procurement Card Program. The Risk Matrix in Appendix B shows the relationship of the specific threats we identified to the controls in place to prevent, eliminate, or mitigate the associated threats.

We also conducted an overall Vulnerability Assessment for the Program. A Vulnerability Assessment shows the relationships among 1) a threat’s inherent risk, 2) the relative strength of the Program’s internal controls, and 3) the Program’s level of vulnerability for each threat and the extent of audit testing required.

We used US Bank electronic information as reported and did not conduct application or data tests on the information provided, as the information was not material to the findings of this report. We reviewed physical files of transactions identified during our review of electronic information.

We used the Government Accountability Office’s definitions of improper, abusive, and fraudulent transactions when classifying questionable purchases.

- Improper transactions are generally purchases intended for City use but are not permitted by law, regulation, or organizational policy.
- Abusive transactions are purchases of authorized goods or services, at terms that are excessive, are for a questionable government need, or both.
- Fraudulent transactions are defined as using the procurement card to acquire goods or services that are unauthorized and intended for personal use or gain.

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**Major  
Accomplishments  
Related To This  
Program**

In Appendix E, the Finance Director informs us of the Procurement Card Program accomplishments.

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## **Finding I**

### **The City's Procurement Card Program Has Weak Internal Controls Which Expose The City To Improper, Abusive, And Fraudulent Uses Of Procurement Cards**

Our audit of the City's Procurement Card Program (Program) revealed several control weaknesses concerning the use, processing, and monitoring of Procurement Card transactions. These control weaknesses expose the City to improper, abusive, or fraudulent uses of procurement transactions. Our limited review of electronic bank information revealed questionable City Cardholder uses of Procurement Cards.

In our Risk and Vulnerability Assessments, we found that the Finance Department (Finance) had no controls or weak controls in place for more than half of the 32 threats we identified. During our limited data testing, we found examples of City Cardholders violating City Procurement Card policies by:

- Splitting purchases to circumvent purchasing limits;
- Purchasing meals in violation of the City Manager's budget freeze on food and meal expenditures;
- Inappropriately procuring services in excess of \$1,000 limitations;
- Making gifts to visiting VIPs using public funds;
- Purchasing from non-City vendors when the City had a Citywide open purchase order from a different vendor;
- Finance processing Procurement Card statements without appropriate Approving Official approval and/or Cardholder signatures;
- Making a personal purchase with a City Procurement Card; and
- Several Retirement Services Department Procurement Cardholders making travel-related transactions that appear to be improper.

In our opinion, Finance should strengthen controls to address the control weaknesses and vulnerabilities we identified, and develop a comprehensive Procurement Card Procedures Manual and use the Manual to advise and train staff who are

assigned Procurement Cards. Further, the City Council's Rules Committee should add an on-going audit of Procurement Cards. Additionally, we recommend that the Federated and Police and Fire Retirement Boards request that the City Council's Rules Committee add to the City Auditor's 2006-07 Audit Workplan, an audit of the Retirement Services Department's travel-related expenses. Finally, the City Administration should develop a policy to guide the purchasing and giving of gifts using public funds.

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**The City Has Significant Exposure Due To A Lack Of Adequate And Documented Internal Controls To Minimize Improper, Abusive, Or Fraudulent Cardholder Uses Of Procurement Cards**

During the course of our audit, we conducted a Risk Assessment of the Procurement Card Program. The rationale for conducting a Risk Assessment is to identify potential threats facing the program or contract under audit and identify the controls or procedures the City has in place to prevent, eliminate or minimize the threats. By so doing, auditors can limit testing and focus on those areas most vulnerable to noncompliance and abuse. During our Risk Assessment, we identified 32 threats associated with the Procurement Card Program. We also identified a lack of corresponding and documented internal control procedures. Appendix B is the Risk Matrix we prepared to identify the Program's threats and corresponding controls. As shown in Appendix B, we assigned an "A" to those Program controls that were reported as actual controls. Any threat without an "A" indicates a complete absence of any control procedures to prevent, eliminate, or mitigate the associated threat.

Of the 32 threats we listed in Appendix B, we found that Finance had no controls or only weak controls in place for 16 of the threats. Specifically, for these 32 threats Finance had no controls in place for five (16 percent), and only weak controls in place for 11 (34 percent). The five threats we identified for which Finance had no mitigating controls are:

- Approving Officials have an unmanageable span of control (responsible for too many Cardholders) and cannot properly oversee Cardholders;
- Cardholder supervisors are not aware of the Cardholder expenditures;
- The City does not receive or control products with unique identifiers (i.e. serial numbers) that Cardholders purchased with Procurement Cards;

- City/department makes late payments for invoices and the City misses opportunities to maximize prompt payment incentives; and
- City departments obtain non-US Bank Procurement Cards or Credit Cards without Finance Department knowledge or approval.

We also found that the Procurement Card Program had only weak controls in place for 11 of the 32 threats we identified (34 percent). The 11 Procurement Card Program threats with only weak controls are:

- Cardholders receive Procurement Cards without credit limits or purchasing restrictions;
- The City/department does not comply with Procurement Card directives (policies, procedures, other guidance);
- Procurement Cards are used by a person other than the person shown on the Procurement Card;
- Cardholders split transactions to avoid purchase limits;
- Cardholders acquire goods and services that are unauthorized and intended for personal use or gain;
- Cardholders make purchases that are not permitted by law, regulation, or policy;
- Cardholders alter documents to legitimize purchases;
- Cardholders make purchases from sources where the City/department has established an open purchase order or the source is restricted;
- Cardholders collude with vendors to provide the City funds for goods and services not provided and the two share the profit;
- Approving Officials and Cardholders collude to misuse Procurement Cards; and
- Cardholders are unaware of the proper use and allowable activities for Procurement Cards.

In addition to the Risk Assessment, we also conducted a Vulnerability Assessment (Appendix C). As the Vulnerability Assessment illustrates, we rated the Procurement Card Program's vulnerability as "moderate to high" or "high" for 66 percent of the 32 threats we identified. In our opinion, the

significant Program weaknesses increase the risk and likelihood of improper, abusive, or fraudulent Cardholder uses of Procurement Cards.

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**Based Upon The  
City Auditor's  
Assessments,  
Finance Agreed To  
Implement  
Improvements To  
The Program's  
Internal Controls**

During our Risk Assessment of the City Procurement Card Program, we found that Finance had inadequate and/or undocumented controls or procedures. We noted that a key control weakness was that Finance did not maintain a Procurement Card Manual for advising and training City staff on the proper uses and restrictions of Procurement Cards. Finance acknowledges the weaknesses and the need to improve controls. To that end, Finance is working proactively to draft a new Procurement Card policy to mitigate some of the threats to the Procurement Card Program. In our opinion, Finance should continue to develop controls to address the identified threats. Those threats include but are not limited to:

- Cardholders obtain Procurement Cards when they don't have a legitimate use for the card;
- Cardholders obtain Procurement Cards without appropriate supervisory approval or knowledge;
- Cardholders receive Procurement Cards without credit limits or purchasing restrictions;
- The City issues Procurement Cards to persons other than active employees;
- The City does not receive the Procurement Card after the employee leaves service or is transferred, and the card remains active;
- Cardholders acquire goods and services that are unauthorized and intended for personal use or gain;
- Cardholders make purchases from sources where the City/department has established an open purchase order or the source is restricted;
- Approving Officials and Cardholders collude to misuse Procurement Cards;
- Cardholders make purchases from vendors where they or the Approving Official have a conflict of interest;
- Cardholders are unaware of the proper use and allowable activities for Procurement Cards;
- Inappropriate transactions are not identified;



- Cardholder supervisors are not aware of expenditures made by Cardholders;
- Approving Officials have an unmanageable span of control and cannot properly oversee Cardholders;
- The City/department makes late payments for invoices and miss opportunities to maximize prompt payment incentives;
- The City is unaware of the total Citywide Procurement Card charges; and
- The City processes payment without appropriate signature approval.

**Control Weaknesses Create An Environment Susceptible To Improper, Abusive, And/Or Fraudulent Procurement Card Purchases**

Our limited review of US Bank electronic procurement information and Finance records revealed that Cardholders of Procurement Cards violated City Procurement Card policies by:

- Splitting purchases to circumvent purchasing limits;
- Purchasing meals in violation of the City Manager's budget freeze on food and meal expenditures;
- Inappropriately procuring services in excess of \$1,000 without purchase orders and making technology purchases without prior approval;
- Making gifts to visiting VIPs using public funds;
- Purchasing from non-City vendors when the City has a Citywide open purchase order with a different vendor;
- Finance processing Procurement Card statements without appropriate Approving Official approval and/or Cardholder signatures;
- A City employee making a personal purchase with a City Procurement Card; and
- Several Retirement Services Department Procurement Card holders making travel-related transactions that appear to be improper.

*Splitting Purchases To Circumvent Purchasing Limits*

We identified that the SJPD split about \$10,500 for 27 digital cameras between five Procurement Cards. The City's Procurement Card procedures limit single purchases to \$2,500 and require Cardholders to follow normal purchasing procedures for expenses above the single purchase limits. Our assessments indicate there is a moderate to high vulnerability of Cardholders splitting transactions to avoid purchase limits.

The five SJPd transactions included three Procurement Cards where one employee was both an Approving Official and Cardholder who was responsible for monitoring and overseeing the use of the two other cards used in the transactions. According to the President's Council on Integrity and Efficiency report, "A Practical Guide for Reviewing Government [Procurement] Card Programs," the monthly review of the Cardholders' statements by the Approving Official is the most important internal control. In these transactions, an Approving Official appears to have violated her duty to oversee Cardholders' compliance with City policies, rules, and regulations and may have involved other Cardholders in order to violate the single purchase limits. In our opinion, the apparent failure of the Approving Official control highlights the need to establish independent monitoring of Procurement Card transactions.

According to the Approving Official, the Local Law Enforcement Block Grant funded the expenditure. The Approving Official identified unspent grant funds that the SJPd would lose if it did not spend the funds. We should note the SJPd should have obtained a City purchase order.

*Purchasing Meals In Violation Of The City Manager's Budget Freeze On Food And Meal Expenditures*

We identified Cardholders using Procurement Cards for meal expenditures that violated the City Manager's meal expenditure restriction. In February 2003, the City Manager implemented an immediate freeze on all meal expenditures. The City Manager informed the City Council that he would consider exceptions in extremely limited cases. Our Vulnerability Assessment revealed a moderate to high vulnerability that Procurement Card Cardholders could make purchases that were not permitted by law, regulation, or policy. Between July 2004 and June 2005, we identified 862 procurement card purchases of meals totaling \$135,000.

In one case, a Cardholder spent over \$900 during a five-day period for lunches at restaurants such as Il Fornaio, The Grill on the Alley, McCormick and Schmick, and Arcadia. The SJPd provided the lunches to eight members involved in the Police Lieutenant Oral Board Process. Finance documentation for those transactions did not include a SJPd justification for an exception to the meal restriction. In our opinion, departments should document a justification for exception to ensure compliance with the City Manager's restriction.

Procurement Card procedures require Cardholders to retain a complete sales draft that includes a brief description of any items purchased and provide the receipt as evidence when reviewing the monthly statement. Finance files included receipts, but the receipts did not include details regarding the food items purchased. These expenses appear to violate the City Manager's restriction on meal expenditures.

*Inappropriately  
Procuring Services  
In Excess Of \$1,000  
Without Purchase  
Orders And  
Technology  
Purchases Without  
Prior Approval*

We also identified that the SJPd used the services of Golden Harvest Restaurant on 27 days from November 2004 to May 2005. The total costs for these services exceeded \$24,000. Many expenses occurred several days apart that, in our opinion, indicated split transactions. Procurement Card procedures prohibit the use of Procurement Cards to obtain services greater than \$1,000. Additionally, this was during the City Manager's freeze on meal purchases.

We reviewed Finance files for five Golden Harvest transactions totaling \$3,800. The receipts in the files did not provide detailed descriptions to indicate what was purchased. These expenditures appear to violate the Procurement Card procedures for services limited to under \$1,000, the City Manager's meal expenditure restriction, and the City's restriction on split purchases.

During the period of our audit, the City Manager required prior approval for technology purchases from the Information Technology Department (ITD) and the City Manager's Budget Office. In some cases, the SJPd submitted requests for approval after the fact without indicating to the ITD that the SJPd had already purchased the requested equipment.

For example, in June 2004, the SJPd purchased over \$940 in computer-related equipment. The SJPd requested authorization to purchase the equipment in August 2004, two months after the fact. The SJPd's email request for these purchases did not state that it had already made the purchases. Email communication among the SJPd, the ITD, and the Budget Office indicated that neither the ITD nor the Budget Office knew that the SJPd had purchased the items prior to requesting and subsequently receiving authorization. Additionally, Finance files did not include any documentation of ITD or Budget Office approval for over \$400 in computer expenses.

*Making Gifts To  
Visiting VIPs Using  
Public Funds*

We found that the Airport Department (Airport) used a City Procurement Card to purchase protocol gifts for visiting VIPs. According to an Airport official, it is standard practice for the Airport to give protocol gifts to dignitaries and airline officials with whom the Airport conducts business. The Airport gave six \$95 Tiffany's key rings to Japanese airport officials and airline executives. On another occasion, the Airport gave three \$180 Mont Blanc pens as gifts to airline executives. Neither the City nor the Airport have a policy on gift giving using public funds. In our opinion, the City Administration should develop a policy to provide guidance on giving protocol gifts to visiting VIPs and dignitaries.

*Purchasing From  
Non-City Vendors  
When The City Has  
A Citywide Open  
Purchase Order  
With A Different  
Vendor*

The City has an open purchase order with Office Max. The City's Procurement Card procedures require Cardholders to use those vendors with whom the City or the Cardholder's department maintains an open purchase order. We found several examples where Cardholders used their Procurement Cards to buy from vendors other than those with whom the City has an open purchase order in violation of Procurement Card procedures. These purchases from non-open purchase order vendors were for items such as CDs and labels.

*Finance Processes  
Procurement Card  
Statements Without  
Appropriate  
Approving Official  
Approval And/Or  
Cardholder  
Signatures*

We identified a number of transactions where Finance processed Procurement Card payments without appropriate Approving Official approval. City Procurement Card procedures require an Approving Official to review monthly statements for accuracy, evaluate the appropriateness of expenditures, ensure adequate documentation, and sign statements authorizing processing. We found numerous examples where Finance processed statements without the assigned Approving Official signature or with unreadable signatures.

For example, we found 18 statements for the SJPd in a single check run where Approving Official signatures were either unreadable or the Approving Official was not the assigned Approving Official. Finance processed payment of these statements without obtaining identifiable or appropriate signatures from the designated Approving Officials. These 18 statements represent about \$16,000 in transactions.

*A City Employee  
Made A Personal  
Purchase With A  
City Procurement  
Card*

We found that a City employee used his City Procurement Card to charge over \$400 worth of car expenses from a Hayward, CA tire and auto merchant. City Procurement procedures expressly prohibit the use of a City Procurement Card for personal purchases. Additionally, the Procurement Cards are specially marked to avoid confusion with personal credit cards.

According to Finance records, the employee reimbursed the full amount 53 days after he made the purchase. A further review of Finance records revealed that the employee did not provide any justification for the personal purchase. According to the employee, he used the City Procurement Card after the merchant was unable to process the transaction with his own personal credit card. In our opinion, the lack of employee training on the proper use of City Procurement Cards contributes to the increased risk of employees violating City Procurement procedures.

**Several Retirement  
Services  
Department  
Procurement  
Cardholders  
Making Travel-  
Related  
Transactions That  
Appear To Be  
Improper**

During our Procurement Card audit, we identified two questionable transactions related to Retirement Services Department (Retirement Services) travel. In the first transaction, a City Procurement Card was used to pay \$400 for point-to-point chauffeured limousine service for a Retirement Services employee. In the second transaction, a City Procurement Card was used to pay for a Retirement Board Member rental car for five days during a personal vacation after attending a Conference. We also found that a Retirement Service employee improperly delegated the use of a City Procurement Card to another employee. While following up on these transactions, we were made aware that Retirement Services obtained the services of an independent travel agent without benefit of a formal procurement process or contractual agreement and maintained a separate airline-issued credit card for procuring air travel services. Government Auditing Standards require that when information comes to the auditors' attention indicating that abuse may have occurred, auditors should extend the audit steps and procedure to, 1) determine whether the abuse occurred, and if so, 2) determine its effect on the audit results. Accordingly, we believe an expanded scope audit of the Retirement Services Department's travel expenditures is in order.

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**Finance Should  
Lead The Effort To  
Strengthen  
Controls To  
Minimize The Risk  
Of Fraud, Waste,  
And Abuse**

We advised Finance that standard internal control practices require that procedures should be written, as simply as possible, and not overlap, conflict, or duplicate other procedures. Finance is developing new Procurement Card policies to address risks and vulnerabilities identified through the City Auditor's Risk and Vulnerability Assessments. Finance took initial steps in addressing the program weaknesses by creating a revised draft policy (See Appendix D). We have reviewed Finance's revised draft policy and provided Finance with some initial comments. We will continue to work with Finance to strengthen the controls for the Procurement Card Program.

The City does not offer Procurement Card training to Cardholders and Approving Officials. Additionally, Finance does not maintain a comprehensive procedures manual to guide or advise Cardholders, Approving Officials, and Finance staff participating in the Procurement Card Program. According to the Government Accountability Office's *Purchase Card Audit Guide*, "management should identify the appropriate knowledge and skills needed in a purchase card program, require the needed training, and maintain documentation evidencing that required training is current for all" employees participating in the purchase card program. In our opinion, the lack of a comprehensive procedures manual and training exposes the City to improper, abusive, or fraudulent Cardholder uses of Procurement Cards.

According to the President's Council on Integrity and Efficiency report, "A Practical Guide for Reviewing Government Procurement Card Programs," the monthly review of the Cardholder's statements by the Approving Official is the most important internal control. During our audit, we found breakdowns in this important control.

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**CONCLUSION**

During the course of our audit, we found that the City's Procurement Card Program had several control weaknesses and vulnerabilities that increase the risk of fraud, waste, and abuse. We identified the Program's lack of adequate and documented internal controls procedures through our Risk Assessment process. The Finance Department agreed to address the identified weaknesses and vulnerabilities. In our opinion, Finance should 1) strengthen controls to address the identified weaknesses and vulnerabilities, 2) develop a procedures manual for the Procurement Card Program to guide employees, and

3) use the procedures manual to advise and train staff on the proper uses and restrictions of Procurement Cards. We also recommend that the City Council's Rules Committee add an on-going audit of the Procurement Card Program and that the Federated and Police and Fire Retirement Boards request that the City Council's Rules Committee add an audit of Retirement Services travel-related expenses to the City Auditor's Annual Audit Workplan. Finally, we recommend that the City Administration develop a policy to guide City officials when giving gifts to visiting VIPs and dignitaries.

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## RECOMMENDATIONS

Based upon our Risk Assessment of the Procurement Card Program and our limited review of Procurement Card transactions, we recommend that the Finance Department:

**Recommendation #1**      **1) Strengthen controls to address the identified weaknesses and vulnerabilities; 2) incorporate in the City's Policy Manual procedures for the Procurement Card Program which provide adequate guidance for employees; and 3) use the procedures to advise and train City staff on the proper uses and restrictions of Procurement Cards. (Priority 2)**

We recommend that the City Council's Rules Committee:

**Recommendation #2**      **Add an on-going audit of the Procurement Card Program to the City Auditor's Workplan. (Priority 3)**

We recommend that the City Administration:

**Recommendation #3**      **Develop a policy to guide City officials when giving gifts to visiting VIPs and dignitaries. (Priority 2)**

We recommend that the Federated and Police and Fire Retirement Boards:

**Recommendation #4**      **Request that the City Council's Rules Committee add to the City Auditor's 2006-07 Audit Workplan, an audit of the Retirement Services Department's travel-related expenses. (Priority 3)**

**Click On The Appropriate Box To View Item**

**Administrator's Response**

**Appendix A**

**Appendix B**

**Appendix C**

**Appendix D**

**Appendix E**